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Approved For Release 2004/11/01 : CIA-RDP75-00793R000300060042-5

OGC 73-0415
13 March 1973

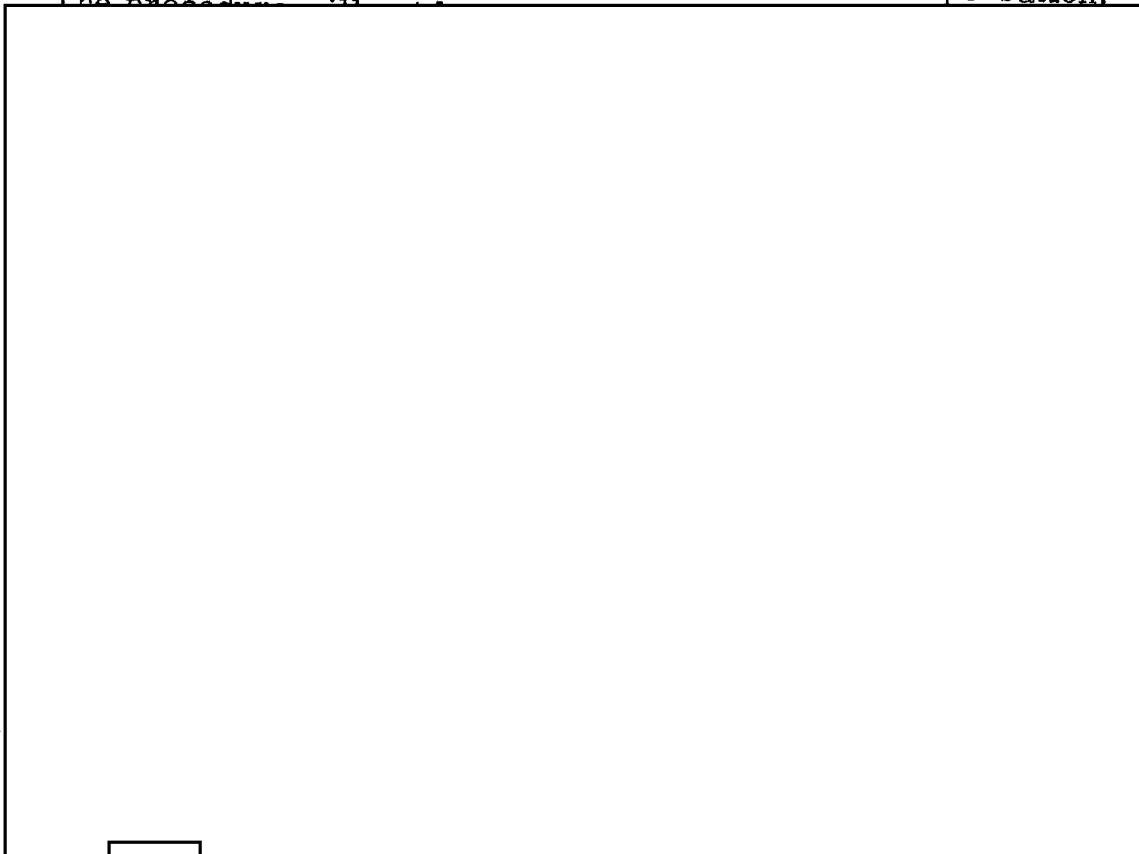
MEMORANDUM FOR: Chief,

25X1A

SUBJECT : Tax Refund Claims for Contributions
to Retirement Systems

1. The IRS fact sheet, dated February 1973 and recently distributed, spells out the procedure to be followed by persons who wish to claim refunds based on the portion of their compensation withheld and contributed to government retirement systems. That procedure should be followed by any employee who wishes to make such a claim, and whose tax return includes such compensation. The procedure...

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OGC Has
Reviewed

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Orig. - Addsee.

Assistant General Counsel

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1-SUBJECT-FEDERAL TAXES

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Contributions to Civil Service Retirement Plans

On April 26, 1972, the Internal Revenue Service ruled (Rev. Rul. 72-250, I.R.B. 1972-21, 6) that the portion of a United States Government employee's compensation that is withheld and contributed to the U. S. Civil Service Retirement and Disability Fund is income in the taxable year withheld and contributed just as if it were paid to the employee directly.

That ruling reiterates the current as well as the long-standing IRS position on this issue based on court decisions and a 1956 ruling (Rev. Rul. 56, 473, C.B. 1956-2, 22). The court cases are cited as Cecil W. Taylor v. Commissioner, 2 T.C. 267 (1943), affirmed sub nom. Malcom D. Miller, et al. v. Commissioner, 144 F. 2d 287 (1944); and Isaiah Megibow, et ux. v. Commissioner, 218 F. 2d 687 (1955).

The IRS position is the same with regard to employee contributions to similar State and local governmental retirement plans.

There is litigation on the issue currently pending before the U.S. Tax Court and a U.S. District court. It is expected that the court cases will be protracted and that the losing parties will appeal. Thus, it may be years before the issue is resolved finally by the courts.

Taxpayers who do not agree with the IRS position and wish to make claim for refund of income taxes previously paid on their contributions to the Retirement and Disability Fund can do so by filing Form 843. In general, Form 843 must be filed on or before April 16, 1973 to claim a refund of taxes paid for the year 1969. Likewise, claims for 1970 must be filed on or before April 15, 1974.

Taxpayers should not reduce income on 1972 income tax returns by deducting or excluding their contributions to the Retirement and Disability Fund. The IRS will identify returns reflecting such deductions or exclusions and process those returns under its "Unallowable Items Program." The reduction in income will not be allowed and any refund otherwise allowable will be delayed.

Instructions for Form 843 are on the reverse side of the form. In completing item "i", which is the amount to be refunded, the taxpayer may insert the exact amount of refund being claimed or "In excess of \$1". In completing item "k", the explanation for the claim, the IRS will accept the following as adequate to cover a claim based on contributions to the U.S. Retirement and Disability Fund:

"Taxpayer, a Federal employee, is entitled to exclude his contribution to the U.S. Civil Service Retirement and Disability Fund from his income for tax year 19-- . I believe the IRS position taken in Rev. Rul. 72-250, I.R.B. 1972-21, 6, is in error."

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ACTION REQUIRED: Please pass to

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1. In response to your queries stated in Para 6 ref, namely, as holder of the second trust, what legal recourse would you have in the event of a default in payment, the General Counsel has pointed out that you, like Avis, would be No. 2 in the scheme of things. As long as the association (the holder of the first trust) were being paid, they would not likely press for foreclosure to satisfy your claim as the second lien holder. You could, however, go to court and get a judgment in your behalf, which would mean that the purchaser could not resell the house until you had been paid off, but this could take up a great deal of time and effort on your part.

2. In either course of action which you mention, namely becoming either the first or second trust holder, you should ask for at least 10% down payment to provide you with an equity cushion.

3. In Para 5 ref, you mention that your realtor will probably not become involved in checking the credit rating of the purchaser. This need not be the case. You can instruct your realtor to obtain a Credit Report on the buyer from a recognized Credit Bureau. The report will cost you about \$35 and will let you be able to judge the buyer's ability to pay both the first and second trusts.

4. The General Counsel suggests your consideration of the following: instead of becoming the holder of a first or second trust on the house, have the purchaser obtain total refinancing for the sale through a bank. At settlement then, your note to the bank of \$15,000 would be paid off first, and the remainder of the purchase price would then be paid directly to you. In this case, the burden would now be on the bank to check out the buyer's credit.

Attachments:

(cont.)

1971 Instructions for Form 1040
Form 1040

IDENTITY SHEET: USC

FEB 1972

Schedules A, B, D, E and R.

4 February 1972

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the General Counsel suggests that your interests be represented in the sale not only by your realtor, but also by a cleared attorney, and suggests using *John*

6. Since you say that your realtor will act as your agent in the sale, we query whether he has Power of Attorney to sign a Deed of Bargain and Sale on your behalf, and whether such Power of Attorney has been recorded among the land records of Fauquier County.

7. In regard to depreciation and Capital Gains Tax, since you say you have depreciated at the straight-line rate, there will be no "recapture of excess depreciation" under Section 1250. Therefore, subtract the total amount of depreciation (over the period of time you owned the house) from the original purchase price of the house, to arrive at the "Adjusted Basis". Then determine the "Adjusted Selling Price" of the house by subtracting from the selling price the amount you have to pay for last minute repairs and improvements, for "points", or for closing costs. Subtract the Adjusted Basis from the Adjusted Selling Price to determine the amount on which you will compute your Capital Gains Tax. Then compute your tax on Schedule D as Long Term Capital Gain. In view of your present salary, it might be wise to compute your tax both by the regular method and also by the Alternate Tax Method (see Pt. 6 on Sched. D), to see if the latter method would save you any money. There is also another method, that of Installment, or Extended Payment. This would apply only if you chose to become the first or second trust holder, and received less than 30% of the selling price in the first year of sale (down payment plus installments). Since you intend to report all of the Capital Gains on your 1972 returns, you might not wish to use the Extended Payment Method.

8. As to your query on how to forward the information, and to whom, you could use regular mail channels and send it to any qualified, reputable CPA in Virginia. If necessary, you could forward the information to Headquarters, where we could compute your tax return in draft, and send it back to you for signature and filing, or you could prepare your return yourself, send it to Hqs. for review (and any adjustment, if necessary), and then Hqs would forward it to IRS.

9. Finally, since you have rented the house for the past seven years, are selling it while still overseas, and are not using the proceeds to buy or build another house, the profit realized from the sale must be reported on Schedule D as long term capital gain, rather than on the special form for reporting profits from the sale of a personal residence.

10. Please inform Hqs. if you require copies of Va. Income Tax forms and instructions.

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27 January 1972

1. I find myself in need of legal assistance pursuant to the sale of my home, and can find no one at my post who might assist me. As it involves a considerable sum, I would appreciate guidance on this matter, the pertinent points of which I have outlined below.
2. I have engaged the services of a realtor who has managed the rental of my private residence in Warrenton, Virginia. Now that I am ready to sell the property, he becomes my agent in this transaction. The unpaid mortgage is in the sum of \$15,000. I wrote him, instructing that I would pay this sum to the Fauquier Savings and Loan Association, whereupon, owning the house outright, I would hold the mortgage which will be written for the future purchaser.
3. Before I was able to effect transfer of the funds to liquidate the mortgage balance, I received a letter from him stating that he advises letting a prospective buyer assume this \$15,000 balance with the loan association, while I hold the second trust-amounting in this case to approximately \$25,000. He sent me estimates of monthly payments: If I held the entire mortgage, the purchaser's monthly payments to me would approximate \$250.00. If such purchaser were to assume the association loan (which incidentally was given at 6%) he would pay to them a monthly sum of \$145.00, and would pay to me, as the second trust holder approximately \$200.00. This total of \$345.00 is a considerable expenditure for the Warrenton area!
4. While it is financially possible for me to liquidate the loan and become the sole mortgagor, the idea of being able to sell the house without further depleting my cash reserves is an intriguing one. Before I choose this course however, I feel I should know what legal rights I have as second trust holder, and if the exercise of such rights in the event of payments default by the purchaser might be both costly and time-consuming.
5. I reason that the loan association, in agreeing to let a second party assume my loan, will be interested only in the ability of that party to meet financial obligations based on a loan of \$15,000. Since my realtor will probably not become involved in any checking of financial solvency, the purchaser approved by the loan association as financially able to assume a \$15,000 loan may be unable to meet the total monthly payments of \$345.00 monthly which both the first and second mortgages will impose upon him.
6. In the event he defaults in the payment of the second trust which I will hold, what will be my course of action, particularly if he continues to pay the association regularly? Would they impede any action on my part to repossess (in an extreme case)? If in your opinion this or any other complication might arise, please advise me accordingly, and I will proceed as originally planned-becoming the sole mortgagor.
7. There is another question with regard to income tax on the sale of this property. As a background, I purchased the house as a private dwelling in 1962, and because of overseas assignments have rented it for a total of 7 years, depreciating it at the straight-line rate. The difference between gross purchase and gross sale price will be approximately \$20,000. I do not intend to use this sum to build another house.

This capital gain will be reported in my 1972 returns, and I would like to ask for advice on how to forward all this information, and to what tax consultant in the U.S. It is difficult for me to know what might be pertinent, and each mutual exchange of correspondence from my post (due to mail service) takes approximately one month. I should like also to inquire if any particular arrangements in down payment received, or terms of loan might make a difference in the tax payment, or if it is based solely on the capital gain difference between purchase and sale price.

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OGC 73-0436
15 March 1973


MEMORANDUM FOR: SB/IO/USSR

SUBJECT :



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1. This is designed to answer the questions raised by  in the informal note hand carried to OGC by your office.

2. We regret the delay in our response. In spite of the references to OGC advice in a dispatch dated 4 February 1972, we have no record of this case, nor does any attorney remember handling it. We cannot prepare your tax return without complete records, particularly in regard to the sale of real estate, and suggest that you prepare it on the basis of your records and the answers to your latest questions which follow. Also forwarded is a copy of IRS Publication 537 which explains in some detail how to report capital gains in the case of installment and other deferred-payment sales.

3. In answer to your question A, you will have to show complete information of the details of the sale to prove qualification for the deferred-payment option. Since you have depreciated the property under the straight line method, there will be no recapture of excess depreciation, but your basis in the property for computing capital gains will have to be adjusted for depreciation taken.



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4. In answer to your question B, interest payments in the case of deferred-payment sales are not taxed as capital gains, and in fact, if less than 4% interest is included in a deferred-payment contract of more than \$3,000, part of the selling price may be considered interest.

5. In answer to your question C, whether or not it will be more beneficial to elect the deferred-payment option or pay the total capital gain tax on your 1972 return, will depend on circumstances and future plans known only to you. To help you in this decision we would point out that the capital gain will be allocated pro rata to the payments received each year under the deferred-payment option, thus giving you a smaller taxable amount each year than if allocated entirely to 1972. More often than not one will pay a smaller tax by using the deferred-payment method. However, depending on the length of the deferred-payment period, your income prospects in those later years and future tax rates which are not predictable, it could, under some circumstances, be better to pay the tax on the entire gain for 1972.

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Assistant General Counsel

Att.

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✓ 1- SUBJECT - FEDERAL TAXES

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1. To assist me in preparing even a rough draft of my 1972 IRS returns (which I will submit to the General Counsel as suggested in), I would appreciate the following information

2. I opted to follow the GC's advice and become the sole mortgagor. I consider using the Extended Payment method for taxation purposes, which I understand is possible, as only 10% of the selling price (down payment and mortgage payments) will be received by December 31, 1972. The following questions have come to mind:

A. It is assumed that the 1972 return must include sale of the property, previous depreciation allowed, and profit from sale to show qualification for the Extended Payment method.

B. Under Extended Payments, is it correct that the down payment received (after fees, etc.) plus mortgage payments should be taxed as Long Term Capital Gains, or must the interest portion of the mortgage payments be taxed differently?

C. Would it be better with my present salary to pay Capital Gains for the entire amount (a profit of \$18,000) in 1972, and in subsequent years be taxed only on the interest portion of the mortgage? (I currently intend to retire in approximately 7 years)

3. I would like to express my appreciation to the General Counsel for the prompt legal advice it has given me in this problem.

Dated 10 November 72
Received 21 Nov 72
Given 10 **25X1A**

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ROUTING AND RECORD SHEET

SUBJECT: (Optional)

FROM:

SB/IO/USSR

4 D 3115

NO.

STATOTHR

DATE

8 December 1972

TO: (Officer designation, room number, and building)

DATE

RECEIVED

FORWARDED

OFFICER'S INITIALS

COMMENTS (Number each comment to show from whom to whom. Draw a line across column after each comment.)

1. General Counsel Office
Attn: [REDACTED]

2.

3.

4.

5. DC/SB/USSR
[REDACTED]

6.

7.

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15.

BY HAND

Lois

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FORM 3-62

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